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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

August 1, 1994

Mr. William Caton
Acting Secretary
Federal Communications Commission
1919 M Street, NW, Room 222
Washington, D.C. 20554

Re: MM Docket No. 93-215
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation

and

CS Docket No. 94-28
Adoption of a Uniform Accounting System for Provision of Regulated Cable Service

Dear Mr. Caton:

Enclosed please find an original and four copies of the Reply Comments of Avenue TV Cable Service, Inc. filed in the above referenced dockets.

Should you have any questions regarding this filing, please contact the undersigned counsel.

Sincerely,

Thomas B. Magee
Counsel for
Avenue TV Cable Service, Inc.

TBM/mcl\avenue\replycom.ltr

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and	)	
Adoption of a Uniform Accounting System for Provision of Regulated Cable Service	)	CS Docket No. 94-28

REPLY COMMENTS OF AVENUE TV CABLE SERVICE, INC.

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August 1, 1994

SUMMARY OF ARGUMENT

As one of the smaller cable operators in this country, Avenue faces greater difficulties than larger operators in attracting capital. The Commission should grant special consideration to the difficulties faced by smaller operators in this area and in others, including the requirement to maintain a Uniform System of Accounts. For purposes of this special consideration, Avenue proposes that "smaller operator" be defined as an operator with 15,000 or fewer subscribers.

The Commission's book value methodology for valuation of rate base is unfair to older operators like Avenue. Avenue suggests that the Commission instead adopt replacement value or market value as an alternative valuation method.

Avenue supports adoption of regulations which will ease the burden on operators called upon to respond to complaints through cost of service showings, by permitting such showings to have longer lasting effect. Additionally, certain procedural changes regarding cost of service showings are needed to ensure that operators are treated fairly in these proceedings. These include requirements (i) that the Commission point out defects and give operators a chance to cure those defects, (ii) that operators be given a chance to respond to any analyses relied upon by the Commission, (iii) that operators be given the option to extend by 90 days the deadline for responding to complaints, and (iv) that operators be permitted to file a new cost of service showing within two years of a previous filing, if so desired.

Finally, the Commission should recognize and adopt the concept that in allocating costs among service tiers, costs should be weighted more heavily on the basic service tier.

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REPLY COMMENTS OF AVENUE TV CABLE SERVICE, INC.

Avenue TV Cable Service, Inc. ("Avenue") by its attorneys, herewith submits its reply comments in the above-referenced proceeding.

Avenue is a privately-owned cable television system servicing the City of San Buenaventura and unincorporated areas of Ventura County, California. Avenue's system provides cable service to 10,537 subscribers.

I. DEFINITION OF SMALL OPERATOR

In several places in these Reply Comments, Avenue indicates that the cost of service rules adopted and proposed to be adopted by the Commission affect smaller operators like Avenue differently from other, larger operators. Avenue requests in these Reply Comments that smaller operators be granted special consideration regarding cost of service filings. As a preliminary matter, for purposes of defining "small operator" or "smaller operator" as used in these Reply Comments, Avenue submits that a reasonable figure is 15,000 customers.

For several reasons defining a small operator as those with 15,000 subscribers or less is justified. First, operators with fewer than 15,000 subscribers do not have the same access to capital that larger operators enjoy. The equity pools developed by large investment companies are unavailable to operators the size of Avenue, as are Libor and other international debt. Second, programming discounts are usually not provided to operators smaller than 100,000 subscribers. Even the most liberal programmers do not provide discounts to operators with fewer than 20,000 subscribers. Finally, cable operations serving less than 15,000 customers are less able to absorb the high level of administrative costs more easily absorbed by larger companies. All of these arguments support the Commission's recognition in the March 30, 1994 Revised Benchmark Order that operators of this size may face higher costs than do other operators.[1] It is for this reason that the Commission granted transition relief to operators of 15,000 or less subscribers.

II. RATE OF RETURN

Several commenters argue that the Commission's presumptive rate of return of 11.25% is too low.[2] Avenue agrees with that assessment.

As the Commission does not yet appear to realize, capital markets treat smaller cable operators like Avenue very differently from other, larger operators.

Avenue believes that its experience in the capital markets is not unlike the experiences of other smaller operators. Like the majority of cable operators smaller than the top 100 in size, Avenue is a locally owned and managed, privately held company. Avenue depends on equity financing for the vast majority of its financing. In contrast to Commission estimates that the debt portion of financing for cable operators will fall within the 40%-70%

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[1] Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, "Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking," MM Docket No. 92-266, at ¶ 118 (released March 30, 1994).

[2] See, e.g., Continental Cablevision, Inc., et al., at 45-52; National Cable Television Association, Inc., at 47-49; Tele-Media Corporation, at 1-5; and Viacom International Inc., at 13-17.

range,[3] Avenue has striven for 10% debt financing and has been successful in achieving 14% debt financing.

Avenue's low debt-to-equity ratio is the result in part of the high cost of debt to Avenue, which is in the range of 10-12% for a company of Avenue's small size and location. Because of its small size, Avenue's ability to attract equity financing is also extremely limited. As such, Avenue must rely for its equity financing on local equity markets. These markets currently provide Avenue with options to obtain equity financing in the 12-15% range.

Given Avenue's low debt-to-equity ratio and its ability to attract equity financing at a rate no lower than the 12-15% range, the Commission's presumption that its overall rate of return should be 11.25% reflects a gross misunderstanding of the financing predicament Avenue and other smaller operators find themselves in. The difficulties of smaller operators in obtaining financing appear to have been all but ignored in this proceeding. As evidence of this disregard, Avenue notes that the rate of return presumptions for smaller operators were based on the experiences of telephone companies or larger cable

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[3] Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation; and Adoption of a Uniform Accounting System for Provision of Regulated Cable Service, "Report and Order and Further Notice of Proposed Rulemaking," MM Docket Nos. 93-215, et al., at ¶ 199 (Released March 30, 1994).

operators, all of whom have access to capital markets unobtainable to smaller operators.

Because smaller operators rely on local markets for their equity financing and lack the capability to find appropriate debt financing, the Commission should revise its rate of return presumptions for smaller operators. Specifically, the Commission should either: (i) increase the current overall rate of return presumption for smaller operators to 15%, adjusted yearly to account for future capital market activity; or (ii) presume that smaller operators will have a rate of return higher than 11.25%, and permit these operators to present a justification for that higher return.

III. RATE BASE

Avenue agrees with comments taking issue with the Commission's method of valuing assets for inclusion in rate base.[4] Avenue agrees with these comments to the extent they argue that net book value is an unfair method for determining the amount on which Avenue may earn its return.

Avenue contends that valuation of rate base using net book value is unfair to older cable operators like Avenue. Avenue began business in 1951. Its cable system was substantially constructed in 1966, well before the onset of

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[4] See, e.g., Continental Cablevision Inc., et al., at 20-23; National Cable Television Association, Inc., at 25-28; Viacom International Inc., at 5-8.

rate regulation, and has been continually rebuilt and updated since that time. Avenue has depreciated these assets over the years so that the current net book value of these assets is small.[5] As a result, Avenue's allowable return on these assets is also small.

To illustrate how the net book value method unfairly treats older cable operators, Avenue's experience may be compared with the experience of a different, hypothetical cable company located in the same county as Avenue which has only recently purchased much of its plant and equipment. For this other operator, the net book value of these assets is relatively high. Although Avenue and the other operator might provide identical services using very comparable facilities, and might labor equally hard to provide those services, the return available to the operator with the recently acquired equipment is much greater than the small return available to Avenue.

In addition, the Commission's insistence on the net book value method for valuation of rate base results in micromanagement of what otherwise would be prudent business decisions, and is in this way contrary to public policy. It is improper for the Commission to allow a regulation that was designed to provide a fair return for cable operators to

[5]The cost to Avenue to construct its cable system in 1966 was approximately $2.9 million. The depreciated basis of its system is now less than $700,000.

have the result instead of dictating how that cable operator should make investments.

Considering these public interest and equity arguments, Avenue suggests alternatives to the net book value valuation method. Adoption of either of these would be preferable for operators like Avenue. These alternatives are:

1. The amount to be included in rate base should be the replacement cost of those facilities, i.e., the amount it would cost Avenue to replace those items.

2. The Commission should use the market value of existing facilities and permit this value to be included in an operator's rate base.

Operators should be provided with a fair return to enable them to upgrade facilities in a timely and efficient manner through use of their own revenue streams. Without a fair return, operators will be constrained to locate funding from other, higher priced sources, thus discouraging these investments from being made at all. The Commission should encourage operators and provide them with the means to invest in and contribute to the development of the information superhighway. Without a fair return, however, operators are unable to make their contribution to this infrastructure.

IV. UNIFORM SYSTEM OF ACCOUNTS

Several operators have opposed the Commission's imposition of a Uniform System of Accounts on cable operators.[6] Avenue supports rejection by the Commission of this requirement. In its place, Avenue proposes that cable operators, especially smaller cable operators such as Avenue, be permitted to use their existing financial accounting records to support cost of service showings, so long as those records conform to Generally Accepted Accounting Principles.

Avenue submits that the Commission proposal, requiring Avenue to tear down and then rebuild existing financial recordkeeping to conform to the Uniform System of Accounts, makes it costly and difficult for Avenue to make any cost of service filing in order to support rates above a benchmark rate. Avenue contends that precluding Avenue and other similarly-situated operators from justifying rates pursuant to a cost of service showing constitutes an abandonment by the Commission of its responsibilities under the 1992 Cable Act to ensure reasonable rates.

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[6] See, e.g., Continental Cablevision Inc., et al., at 63-65; Falcon Cable TV, at 4-11; National Cable Television Association, Inc., at 49-55; Tele-Communications, Inc., at 20-24; Time Warner Entertainment Company, L.P., at 19-21.

In the Rate Order,[7] the Commission recognized that the benchmark regulation approach would be inappropriate for some cable systems and that benchmark rates for these systems might not allow operators to recover their costs and continue to attract capital. The Commission determined that Congress intended a different, better result for cable operators. To this end, the Commission permitted operators unsatisfied with their benchmark rates to justify higher rates through a cost of service showing.[8]

Despite these Commission pronouncements and despite this declared Congressional intent, the Commission's insistence in the March 30, 1994 Cost of Service Order that all cable operators employ a Uniform System of Accounts has made the cost of service "safety-valve" option cumbersome for Avenue and for smaller operators like Avenue. This is true because vast amounts of time and expense are required to conduct such an overhaul of Avenue's financial accounting system. In order for Avenue to conform to the Uniform System of Accounts, Avenue would need to break down every item in its chart of accounts to its lowest accounting level and subsequently reassign each of these accounting bits to the proper place in the Uniform System of Accounts. Avenue

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[7] Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992; Rate Regulation, "Report and Order and Further Notice of Proposed Rulemaking," 8 FCC Rcd 5631, MM Docket No. 92-266 (released May 3, 1993).

[8] Id. at 5794, ¶ 262.

has determined that such a cumbersome, expensive undertaking is difficult to justify given the labor-hours required and the size of its workforce.

Thus, in proposing the Uniform System of Accounts, it appears again that the Commission has not given enough consideration to the disproportionate burdens imposed on smaller operators like Avenue. Adoption of a system of accounts based on a model employed by large telephone companies is inappropriate for the cable industry and is wholly inappropriate for cable operators the size of Avenue. This is true regardless of any endorsement of this proposal by the telephone industry.[9]

To ensure that the Commission fulfills its statutory responsibilities, the Commission should not apply the uniform accounting system, at least for smaller operators for whom such a system is infeasible. To provide Avenue with a viable cost of service alternative, Avenue must be permitted to justify its rates using existing accounting records.

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[9] See Bell Atlantic, at 7-9; GTE Service Corporation, at 10-11.

V. COS FILINGS IN RESPONSE TO COMPLAINTS

At least one set of commenters has addressed the issue of cost of service filings to be made in response to complaints.[10] On this issue, Avenue supports adoption of regulations that ease the burden on operators who may be called upon to justify rates through cost of service showings. Specifically, Avenue proposes that operators who have made cost of service filings with the Commission, and who have refrained from any increase in rates since that filing, not be required to make any additional cost of service showing as the result of a complaint. It is unnecessary to subject operators to the ordeal of establishing anew cost of service rates which likely will reflect little difference from rates already approved by the Commission pursuant to a previous filing. In the alternative, if the Commission deems it necessary that an operator make a cost of service filing in response to a complaint, Avenue proposes that such filing suffice to defend any future complaint for a period of two years. During this two year period, the operator may not be compelled to justify its rates with another cost of service filing.

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[10] See Continental Cablevision, Inc., et al., at 67-79.

VI. PROCEDURAL RECOMMENDATIONS

Continental Cablevision, et al., make several procedural recommendations regarding cost of service showings which Avenue believes are necessary to ensure that operators are treated fairly in these proceedings by the Commission.[11]

First, Avenue agrees that the Commission should be required to point out defects in cost of service filings and provide an opportunity for operators to cure those defects. The Commission is in a better position than operators, especially smaller operators, to understand how to comply with its rules. This is true because the Commission has drafted the regulations and will have reviewed vast numbers of compliance filings. In determining whether to grant this request, the Commission should bear in mind that in almost all cases, the cable operator completing the forms is not as sophisticated about the form's requirements as the Commission.

Second, Avenue agrees that if the Commission relies on any analyses in setting an operator's rates, those analyses should be provided to the operator and the operator should be given an opportunity to respond. In a cost of service proceeding which already is hazardously abbreviated, and which has at stake the livelihood of Avenue and its employees, it is only fair that Avenue be given an

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[11] See Continental Cablevision, Inc., et al., at 73-79.

opportunity to examine such extrinsic evidence. Moreover, the comments of cable operators on these analyses will be useful to the Commission in pointing out shortcomings and in examining whether the analyses in question are relevant to that operator.

Third, Avenue agrees that if an operator's rates are challenged through a complaint, the operator should be able to extend by ninety (90) days the date by which any required cost of service justification would be due. Thirty (30) days is an insufficient amount of time for any operator to assemble an adequate cost of service presentation.

Finally, Avenue agrees that if an operator is required to justify its rates through a cost of service showing, the operator should not be precluded from filing another cost of service justification for two years. Although cost of service showings are difficult to make, circumstances may change so that Avenue may wish, for any number of legitimate reasons, to seek a rate increase during that two year period. It is unfair in this instance to preclude Avenue from justifying those increased rates using the cost of service methodology.

VII. COST ALLOCATION AMONG SERVICE TIERS

Continental, et al. introduce the concept that cost allocation among service tiers should be designed so that a plant's usage is more fairly allocated among those tiers.[12] Avenue believes that cable operator costs should be more heavily weighted on the operator's basic service tier, and that this concept should be recognized and adopted by the Commission in its cost of service rules.

Providing that costs be weighted more heavily on the basic tier is justified for a number of reasons. First, it is undeniable that the channels comprising the basic service tier are generally the more "valuable" channels, such as the major networks. These channels are in fact required to be carried by the Cable Act. Second, Tier 2 service could not be offered without basic services. Finally, most of Avenue's costs, such as those for underground cable, for labor, for overhead, etc., are necessary to supply basic service. In fact, in the case of Avenue, all of its plant was built to provide basic service alone, since Tier 2 was not begun until after its plant was built. For all of these reasons, the Commission should recognize and adopt a weighing system that results in greater allocation of costs to basic services.

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[12] See Continental Cablevision, Inc., et al., at 26-28.

VIII. CONCLUSION

Avenue respectfully requests that the Commission adopt the recommendations set forth herein, recognizing the special circumstance of smaller, older operators, and recognizing that certain of these changes are more fair for all cable operators filing cost of service showings.

Respectfully submitted,

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August 1, 1994
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CERTIFICATE OF SERVICE

I, Marianne C. Lynch, certify that I have this 1st day of August, 1994, sent by regular United States mail, postage prepaid, a copy of the foregoing "Reply Comments" to:

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